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FEDERAL INCOME TAX 1943—SPECIAL BENEFITS TO MEMBERS OF THE ARMED FORCES¹

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A. SCOPE AND PRACTICAL IMPORTANCE

On June 9, 1943, with the enactment of "The Current Tax Payment Act of 1943,"² the serviceman became a taxpayer in a class by himself. Previously there were special benefits in favor of the serviceman, but now, for the year 1943, even the method of computing tax is entirely different for servicemen than it is for civilians.

The reason why this subject should be of special interest to attorneys is that the present law affords a great opportunity for substantial tax savings and refunds in favor of servicemen for 1943. Thus, substantial refunds will be available for most servicemen who had a moderate or large earned income in 1942. Suppose, for example, that a single doctor earned \$16,000 net income in 1942 and entered the Army as a captain in January, 1943. In March, 1943, he paid his full 1942 tax of approximately \$5,000. Under the present law he would, under normal circumstances, be entitled to a refund of nearly the whole \$5,000. Also, most married couples who reported a substantial tax for 1942 on separate returns will be able to save tax by now filing amended returns. This is illustrated by the case of a husband and wife who filed separate returns in March, 1943, on the long return form 1040, each taking \$600 of the \$1,200 personal exemption. The man then enters the service early in 1943. Assuming that they do not avoid the tax entirely, they can ordinarily save in the neighborhood of \$200, by now amending their 1942 tax returns to let the wife claim the full \$1,200 exemption, and later file separate 1943 returns with the husband taking the full \$1,200 exemption or so much of it as is necessary to result in the least total tax. Proportionately more would be saved by this procedure if the husband claimed more than \$600 of the personal exemption on his 1942 return.

In spite of the importance of the special provisions relating to servicemen, they are quite commonly misunderstood or unknown to many members of the armed forces, their wives who are at home, and even to many lawyers who do not specialize in income tax matters. Such publicity as has been issued has attempted to simplify for public consumption a subject which cannot be both simplified and accurate at the same time. Also the Treasury Department instructions and forms issued for

¹ Pursuant to Article 113(2) U. S. Navy Regulations, the opinions or assertions contained herein are the private ones of the writer and are not to be construed as official or reflecting the views of the Navy Department or the naval service at large.

² Pub. L. No. 68, 78th Cong., June 9, 1943.

use in preparation of September estimates, although admirably simplified for civilians, were not adapted to use by most servicemen.

It is the aim of this article to list the special benefits and provisions relating to servicemen, so as to be currently useful to attorneys in the preparation of tax declarations and returns, with a resulting benefit to the servicemen and their wives who are clients. It is not the intent of the writer to solve the mystery of why the law was written in its present form.

At the time of writing this article, it appears quite certain that Congress will simplify the tax law and perhaps increase the rates, but it does not seem likely that the present benefits in favor of servicemen will be reduced, at least for the year 1943. In any event, a taxpayer's present course of action must be guided by the law as it exists, and a present knowledge of the existing provisions will certainly simplify an understanding of the consequences of such amendments as may be made.

Although the provisions benefitting servicemen which are most commonly misunderstood are those relating to the right to recompute the 1942 tax (discussed in Sections G and H, *infra*), it has been deemed preferable to first discuss the special provisions relating to exclusions, special allowances and deductions, because a knowledge of them is necessary in the preliminary steps of tax computation.

B. DEFINITION OF ARMED FORCES AND ACTIVE SERVICE

As used in this article the word "serviceman" will include the military and naval forces of the United States and may include the military or naval forces of other United Nations if the particular provisions of the income tax law under discussion include such forces. Ordinarily the military and naval forces of the United States include (but are not necessarily limited to) the Army, the Navy, the Marine Corps, the Coast Guard, the Army Nurse Corps, female, the Navy Nurse Corps, female, the Women's Army Corps (the "WACS"), the Women's Reserve Branch of the Naval Reserve (the "WAVES"), the Women's Reserve Branch of the Coast Guard Reserve (the "SPARS"), and the Marine Corps Women's Reserve. With respect to postponements, however, the phrase also includes commissioned officers of the Coast and Geodetic Survey and of the Public Health Service. The term "active duty" or "active service" ordinarily includes all service, irrespective of whether it is in the field or theater of war, and includes periods during which a person is absent from duty on account of sickness, leave, internment by the enemy or other lawful cause. However, personnel in the inactive reserve or on retirement are not in active service.

For purposes of the Soldiers and Sailors' Civil Relief Act, the definition of military service includes training or education under the supervision of the United States preliminary to induction into the military service.

C. ITEMS OF PAY WHICH ARE INCLUDED AND EXCLUDED FROM GROSS INCOME

One of the many surprises which a civilian discovers upon entering the service is that only about two-thirds of his government pay is included in taxable gross income for income and victory tax purposes. Some items of pay are specifically declared non-taxable by the statutes which provide for them. Other items are in the nature of gratuities and therefore non-taxable as gifts under Section 22 (b) (3) of the Internal Revenue Code. However, for purposes of brevity and usefulness of this article, a check list of the common items of service pay will be of more value than a discussion of the reasons why each item is or is not taxable. Such a check list follows below:

(a) *Items Included in Gross Income:*

The following are the most common specific items paid or furnished to members of the military and naval service which are to be included in gross income for tax purposes:

1. Base pay.³

³ Although space does not permit a list of the base pay rates of all of the various armed forces, the following table of Navy pay and allowances may be of interest:

Rank:	Allow. with Depndts.:		
	Base Pay	Rental	Subsistence
Admirals	\$666.67	\$120	\$42
Vice admirals	666.67	120	42
Rear admirals (upper half)	666.67	120	42
Rear admirals (lower half)	500.00	120	42
Commodores and captains	333.33	120	42
Commanders, over 30 years	333.33	120	42
Under 30 years	291.67	120	63
Lieutenant commanders, over 23 years	291.67	120	63
Under 23 years	250.00	105	63
Lieutenants, over 17 years	250.00	105	63
Under 17 years	200.00	90	42
Lieutenants (j. g.), over 10 years	200.00	90	42
Under 10 years	166.67	75	42
Ensigns, over 5 years	166.67	75	42
Under 5 years	150.00	60	42
Commissioned warrant officers,			
Over 20 years, creditable record	250.00	105	63
Over 10 years, creditable record	200.00	90	42
Under 10 years	175.00	75	42
Midshipmen	65.00		
Warrant officers	150.00	60	42

ENLISTED MEN

Classification:	Base Pay
Chief petty officers with permanent appointments	\$138
Chief petty officers with acting appointments	126
Petty officers, first class	114
Stewards, first class	114
Cooks, first class	114
Petty officers, second class	96
Stewards, second class	96
Cooks, second class	96
Musicians, first class	96
Petty officers, third class	78
Firemen, first class	78
Stewards, third class	78

2. Longevity pay. This constitutes certain percentage additions to base pay which are made according to the length of service of the person in question.
3. Extra compensation for special duty (aviation, foreign duty, parachute, sea duty, submarine, etc.). For such special duties further additional percentages are added to base pay.
4. Retirement pay where retirement was for age or service or for sickness or injury not incurred in line of duty.
5. Mileage (report entire amount received as gross income and deduct necessary traveling expenses, actually paid, such as meals, railroad fares, lodging, etc.). Where optional form of work sheet or return is used, include as a part of gross income only the amount of mileage in excess of actual expenses.
6. Travel pay to discharged enlisted men (report in the same manner as mileage).
7. Transportation of families of officers and enlisted men (the actual cost of such transportation to the Government is considered taxable income to the serviceman. No deduction allowed.).
8. Interest on deposits of enlisted men.
9. Additional pay for special qualifications in use of arms.
10. One year's pay received by officers wholly retired.
11. All permanent and transient additions to pay (enlisted men).
12. Money allowances received by retired enlisted men under acts of March 2, 1907 (34 STAT. 1217) and June 30, 1941 (55 STAT. 394) (Public Law 140, 77th Cong.) [prior to their repeal as to allowances by section 19 of the Pay Readjustment Act of 1942], in lieu of rations, clothing, quarters, fuel and light.
13. Enlistment allowances paid to honorably discharged enlisted men who reenlist.
14. Extra pay received as holder of Medal of Honor, or the like.
15. Extra pay to enlisted personnel from post exchanges, ship's service, etc. Certain enlisted personnel, such as barbers, are assigned to additional duty with post exchanges and ship's service departments. Post exchanges and ship's service departments although considered governmental instrumentalities, are self-sustaining and sell articles of common use and services such as barber shop, clothes

<i>Classification:</i>	<i>Base Pay</i>
Cooks, third class	78
Aviation cadet	75
Nonrated men, first class, (except firemen, first class and musicians, first class)	66
Firemen, second class	66
Musicians, second class	66
Nonrated men, second class (except firemen, second class and musicians, second class)	54
Firemen, third class	54
Nonrated men, third class (except firemen, third class)	50

Allowances (Per Day Basis)

Quarters—\$1.80 paid all enlisted men not furnished Government quarters; additional \$1.25 paid men of first three pay grades for dependents prevented by orders of competent authority from living with them and not furnished Government quarters.

Subsistence—\$1.00 paid aviation cadets not subsisted at Government expense; \$1.50 paid all other enlisted men not subsisted at Government expense or furnished Government messing facilities.

Government contribution to family allowances, monthly basis—Wife alone, \$28; wife and one child, \$58, with \$20 for each additional child; no wife but one child, \$20, with \$20 for each additional child; Alnav. 175.

pressing, etc., to servicemen. They pay enlisted men, who are employed by them, compensation in addition to their regular Army or Navy pay.

Persons in the service make allotments from pay to their dependents and for insurance, war bonds and savings. Such allotments are the same as wage assignments and do not in any way affect taxable income even though the pay check received is consequently less as a result of the amounts withheld due to such allotments. The same is true of the portion of monthly family allowances which is chargeable against enlisted men's pay under the Service Men's Dependents Allowance Act of 1942. (Pub. L. Nos. 625 and 705, 77th Cong., 2d Sess. Increase of family allowance under Senate Bill 1279, 78th Cong. was enacted October 26, 1943.)

The Finance Officer or Disbursing Officer, who carries the payrolls of the particular serviceman in question, has to date been required to give to the serviceman a statement at the end of the year which shows the taxable pay received during the year. For purposes of estimates, an attorney can check the probable pay of a serviceman of a particular rating, length of service, and special duty by phoning to the Finance Officer or Disbursing Officer of the nearest Army or Navy activity.

(b) Items Excluded from Gross Income:

The following are the most common specific items paid or furnished members of the military and naval service which are to be excluded from gross income for tax purposes:

1. Value of subsistence and quarters furnished in kind.
2. Money rental allowance where quarters are not furnished in kind. (Applicable to Army, Navy, Coast Guard, Coast and Geodetic Survey, and Public Health Service.)
3. Money subsistence allowance where subsistence is not furnished in kind.
4. Value of travel furnished in kind to discharged enlisted men.
5. Per diem allowance in lieu of subsistence paid to an officer traveling on official business away from post of duty. It is immaterial in this connection whether he does or does not maintain a home while in travel status, since his per diem is an "allowance" and not "compensation."
6. Uniforms furnished in kind to enlisted men.
7. Uniform gratuity or allowance paid to officers, nurses, or enlisted personnel.
8. Money allowance paid upon discharge to enlisted men, in lieu of unused clothing allowance to their credit.
9. Amounts contributed by Government to serviceman's "monthly family allowance" are gifts and need not be reported by members of the family receiving them. Contributions to the family allowance by the serviceman through deductions from his pay need not be reported by the family, but are a part of his pay and are included in his gross income.
10. Gratuity pay (six months' pay to beneficiary of a deceased officer or enlisted man).
11. Gratuitous medical or hospital treatment provided by Government in government hospitals.
12. Benefits and pensions received under World War Veterans' Act, 1924 (43 STAT. 607), World War Adjusted Compensation Act

- (43 STAT. 121), act of August 12, 1935 (49 STAT. 607) (Pub. L. No. 262, 74th Cong.), or war risk insurance acts.
13. Pensions received from the United States by the family of a veteran, for services rendered to the United States in time of war, are exempt as gifts.
 14. Retired pay of persons retired from service for physical disabilities incurred in line of duty. (INT. REV. CODE § 22(b)5; Rev. Act. of 1942, § 113.)
 15. Amounts received in reimbursement for losses, sustained by officers, nurses, and enlisted men, in foreign countries, due to appreciation of foreign currencies in the relation to the American dollar, as authorized by the act of March 26, 1934 (48 STAT. 466), and by Executive Order dated September 15, 1938, as amended.
 16. Personal cash allowance received by admirals and vice admirals.

D. SPECIAL \$1,500 ALLOWANCE FOR MEMBERS OF ARMED FORCES⁴

The preceding section indicated that certain specific items of service pay are not considered gross income for tax purposes. An additional and even more substantial benefit is that even that part of active service pay, which would otherwise be taxable, need now be reported as gross income only to the extent to which it exceeds \$1,500. This is the result of a special allowance up to \$1,500 which was provided by section 7 of the new law, which reads as follows:

"Section 7. Additional Allowance for Members of Armed Forces.

"(a) In General.—Section 22(b)(13) of the Internal Revenue Code (relating to additional allowance for military and naval personnel in computing net income) is amended to read as follows:

"'(13) Additional Allowance for Military and Naval Personnel.—In the case of compensation received during any taxable year and before the termination of the present war as proclaimed by the President, by a member of the military or naval forces of the United States for active service in such forces during such war, or by a citizen or resident of the United States who is a member of the military or naval forces of any of the other United Nations for active service in such forces during such war, so much of such compensation as does not exceed \$1,500.'

"(b) Effective Date.—The amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1942."

The wording of the law is such that the above allowance applies both for regular income tax and the victory tax purposes. It is granted beginning with the tax year 1943, and it is in addition to the regular personal exemptions. It is not a personal exemption, but is in the nature of a general exclusion and applies only with respect to "compensation * * * for active service * * *." In view of the fact that it is

⁴ Regulations in T. D. 5297, Sept. 20, 1943 (FED. REG., Sept. 23, 1943, p. 12930).

an exclusion, the fact that it is claimed will not appear upon the face of the tax return, but its benefit is obtained by reporting as income only the excess of such compensation over \$1,500.

In the case of community income, the Commissioner of Internal Revenue has ruled⁵ that the allowance of \$1,500 of active service pay is to be excluded before dividing income between husband and wife. Thus, if an officer, domiciled in a community property state, had active service pay of \$2,500, he and his wife using separate returns would each report one-half of the excess over \$1,500, or \$500 apiece.

The \$1,500 exclusion does not apply to active service pay received after the taxpayer has been discharged from active service, because the law limits the allowance to active service pay "received * * * by a member of the military or naval forces."

E. ADDITIONAL ALLOWANCE FOR MILITARY AND NAVAL PERSONNEL (1942 ONLY)

The \$1,500 allowance discussed under the preceding heading replaced a \$250 and \$300 special allowance, which was applicable only for the taxable year 1942 and was in favor of only those military and naval personnel who were below the rank of commissioned officer. In view of the fact that it may still be necessary to prepare 1942 returns for some of the servicemen whose tax returns were postponed, the former section 22 (b) (13) (Revenue Act of 1942, § 117) is quoted below for information:

"Sec. 117. Additional Allowance for Military and Naval Personnel.

"Section 22(b) (relating to exclusions from gross income) is amended by adding at the end thereof the following new paragraph:

" '(13) Additional Allowance for Military and Naval Personnel.—So much of the amount received, before the termination of the present war as proclaimed by the President, by personnel below the grade of commissioned officer in the military or naval forces of the United States as salary or compensation in any form from the United States for active service in such forces during such war, as does not exceed \$250 in the case of a single person and \$300 in the case of a married person or head of a family. The determination, for the purpose of this paragraph, of the taxpayer's status in the armed forces and his family status shall be made as of the end of the taxable year.' "

F. DEDUCTIONS

There are no special deductions, in favor of servicemen, but they are determined on the same principles as deductions allowed to other taxpayers using the long return form 1040. However, a list of some of the most common military and naval expenses may be useful. It is

⁵ T. D. 5297, *supra* note 4.

noted that compensation received from the United States by its military and naval personnel represents income from a business for tax purposes.

Deductions Allowable

(a) Business expenses:

1. Dues to professional societies.
2. Subscriptions to professional journals.
3. Expenses for use of personal automobile on official business if an official car is not available and if necessity for such use can be shown conclusively.
4. Expenses incurred in travel for which mileage allowance is reported as part of gross income.
5. Depreciation on capitalized cost of providing horse and essential equipment, where Government requires officer to provide his own mount used exclusively in official duties.
6. Payment for premium on a bond (when required by the Government of an individual as a protective measure).
7. With respect to the cost of equipment which is required of military or naval personnel, the Bureau of Internal Revenue allows a deduction only for those items of equipment which do not replace articles required in civilian life, such as epaulets, aiguillettes, campaign bars, collar ornaments, corps devices, Sam Browne belts, sword, sword belt (dress and undress) and sword knot.

It is possible that a change in the Bureau's policy will be made sometime in the future in view of recent tax court decisions which tentatively indicate that a deduction may be allowable for uniforms even though they replace articles required in civilian life.

See: *Harsaghy v. Commissioner*, July 30, 1943, 2 T. C. No. 58. *Meier v. Commissioner*, July 21, 1943, 2 T. C. No. 55. *Benson v. Commissioner*, June 1, 1943, 1 T. C. No. 2.

8. Mess bills afloat—A naval officer while on permanent duty afloat who actually maintains a home elsewhere is entitled to deduct only the difference between amount expended for mess bill and the amount of his subsistence allowance. For example: An officer with dependents receiving subsistence allowance of \$18 per month and who pays a mess bill of \$30 per month is entitled only to a deduction of \$12 for each month. The existence of a "home" is a question of fact to be determined in each individual case (to the satisfaction of the Commissioner of Internal Revenue). If an officer does not have a "home," the difference between amount paid for mess bill and subsistence allowance received is not allowed as a deduction.

(b) Losses:

1. Incurred in trade or business (not insured).
2. From fire, storm, shipwreck, theft, or casualty (not insured).
3. War loss of property by military or naval operations or under enemy control.
4. Loss of disbursing officers due to shortage but not result of negligence.

(c) Alimony:

Periodic payments (including amounts chargeable to an enlisted man's pay under the Servicemen's Dependents Allowance Act of 1942) by a husband to a divorced or legally separated wife subsequent to a

divorce or separate maintenance decree in discharge of a legal obligation incurred by him under such decree or under a written instrument incident to such divorce or separation. (INT. REV. CODE § 23 (u); Revenue Act of 1942, § 120 (b).)

Deductions Not Allowable:

1. Uniforms—(Cost of uniforms held to be in the nature of personal or living expenses. No deduction is allowed on account of depreciation or obsolescence of uniforms.)
 - (a) Items of equipment such as gold lace, chin strap, gilt buttons, gilt and silver devices on caps, and gold lace and gilt buttons on the uniforms are considered a part of the uniform and cap which take the place of regular clothing, and the cost thereof may not be deducted, but see item (a) 7 of allowable deductions, *supra*.
 - (b) The cost of altering the equipment on a uniform subsequent to promotion or demotion is a personal expense and not deductible.
2. Loss of pay by sentence of court martial.
3. Hospital fund deductions from pay.
4. Cost of packing, crating, freight, etc., in changing official station, attributable to personal effects of members of officer's family.
5. Dues to officers' clubs.
6. Premiums paid on war risk, converted Government or commercial policies, life insurance policies, and premiums paid for increased insurance to cover hazards of aviation duty.

G. COMPUTATION OF TAX FOR 1943—SPECIAL RULES
APPLICABLE TO SERVICEMEN

1. *The Existing Misunderstandings.*

The most commonly misunderstood effect of the new tax law is the special method of computing the 1943 tax for servicemen. It is seriously doubted whether it has been clearly understood by any individual, other than the lawyers and accountants who have absorbed it by experience. This is not a flattering reflection upon those who are responsible for drafting the income tax laws, but it may be a blessing in the long run by resulting in pressure for eventual simplification of future tax laws.

Many members of the armed services, and their wives, who formerly made out their own returns, will turn to lawyers for advice. It is hoped that this article may be of some assistance by setting forth a step-by-step method of tax computation, together with comments upon the facts which should be kept in mind in computing tax. Although this article may be a reminder of the principles involved, it is respectfully suggested that a lasting understanding can only be acquired by the actual practice of preparing the tax declarations or returns themselves.

2. *Total 1942 and 1943 Tax for Civilians Compared with Total 1942 and 1943 Tax for Servicemen.*

The method of computation of tax, for all individual taxpayers for

1943,⁶ is different than it has been or will be for any other year. This is the necessary result of the fact that the purpose of the Current Tax Payment Act⁷ was to put all taxpayers on a current "pay-as-you-go" basis without forgiving entirely the tax for either 1942 or 1943. The technical method of achieving the desired result was to discharge all 1942 tax liability as of September 1, 1943, and to provide certain additions to what would be the 1943 income and victory tax if computed in the usual manner.^{7a} The applicable provisions are set forth in section 6 of the Act.⁸

Civilians:

As a result of paragraphs (a) and (b) of Section 6 of the Act, *civilians* pay tax for the higher of the two years 1942 and 1943, plus an addition of 25 per cent of the tax for the lower year where such tax is \$66.67 or above. If such lower tax is less than \$66.67, only the amount by which it exceeds \$50, if at all, is added. The above mentioned addition is not reported on the declarations of estimated tax, but will be shown on the annual return due March 15, 1944.

Servicemen:

Servicemen will pay according to the same formula as civilians, *only* if their 1943 income and victory tax (computed in the usual manner without reference to other years) is greater than the tax shown on their 1942 returns. Where their 1942 tax is greater,⁹ however, servicemen have the benefit of the amazing¹⁰ Section 6(d)(1) of the Act, which reads as follows:

⁶ The effect of forgiveness does not apply to taxpayers guilty of certain criminal offenses or fraud for the year 1942. § 6(a) and 6(b) of Current Tax Payment Act.

⁷ Pub. L. No. 68, 78th Cong., June 9, 1943.

^{7a} In cases where the 1942 tax is higher than the 1943 tax, the law itself and the Treasury regulations say that the 1943 tax is increased by "the excess of the tax for * * * 1942 over the tax for * * * 1943." It seems to the writer that the result is much simpler to comprehend by saying that where the 1942 tax is higher, the 1942 tax is to be paid. Therefore, throughout this article it has been so expressed.

⁸ Outside of the scope of this article is paragraph (c) of § 6 which provides for an additional increase of tax in cases where the surtax net income of the taxpayer for 1942 or 1943 is more than \$20,000 greater than the surtax net income for a base year to be selected by the taxpayer from the years 1937, 1938, 1939 or 1940. Also special provisions are made by § 6(d) (3) (4) and (5) with respect to foreign tax credits, compensation for services rendered over a period of more than 36 months, and to income derived from a business formerly operated under the corporate form. Regulations covering these provisions, and covering changes of status during the tax year, are set forth in T. D. 5300, October 1, 1943 (Fed. Reg., Oct. 5, 1943, at p. 13452, *et seq.*).

⁹ The 1942 tax of servicemen ordinarily will be greater than 1943 due to the \$1,500 additional allowance from 1943 service pay under § 7(a) of the Act, *supra* p. 187.

¹⁰ The benefit of § 6(d) (1) applies even to a taxpayer in active service for but one day in 1942 or 1943. The recomputation of 1942 tax may be made with respect to all earned 1942 income from whatever source, and is not limited to service pay. Thus, a taxpayer with a \$14,000 salary for 1942 and a \$3,000 salary for 1943 would gain a tax benefit of about \$5,000 by entering the armed services on December 31, 1943. The benefit could be considerably greater in the case of a person in the higher tax brackets.

"Sec. 6(d)(1)

"Application of Subsection (b) to Members of Armed Forces.—If the taxpayer is in active service in the military or naval forces of the United States or any of the other United Nations at any time during the taxable year 1942 or 1943, the increase in the tax for the taxable year 1943 under subsection (b)(1) shall be reduced by an amount equal to the amount by which the tax for the taxable year 1942 (determined without regard to this section) is increased by reason of the inclusion in the net income for the taxable year 1942 of the amount of the earned net income (as defined in section 25 (a)(4))."¹¹

The effect of the above provision is that where the 1942 tax of a serviceman was higher than his 1943 income and victory tax (computed without the benefit of this section), the serviceman may recompute his 1942 tax eliminating earned net income. If after such recomputation his 1942 tax is still higher than the 1943 tax, the recomputed 1942 tax is paid. If it is less, then the 1943 tax is paid. Also in all cases where the original 1942 tax (before recomputation) of the serviceman was the higher, 25% of the 1943 tax is added, except that where the 1943 tax is less than \$66.67, then only the amount by which it exceeds \$50, if at all, is added. This 25% addition is not reported on the declarations of estimated tax, but is included in the annual return due March 15, 1944.

If the 1942 tax, even after recomputation, is still higher than the 1943 tax, servicemen have another tax saving opportunity which is also available to civilians. Only 25% of increase in 1943 tax (so long as they do not raise the 1943 tax up to the amount of the 1942 tax) will be payable, as distinguished from 100% if the 1944 tax should be increased. Therefore, in such a case, it is preferable to take capital gains and obtain other income before the end of 1943, but postpone deductible expenses until 1944.

3. Step-by-Step Formula for Computing Total 1942 and 1943 Tax.

The steps involved and the amount of total tax to be paid for 1942 and 1943 can probably best be illustrated by a formula, as follows:

¹¹ For purposes of the above provision, T. D. 5300, Oct. 1, 1943 (FED. REG., Oct. 5, 1943, p. 13458) defines members of the armed forces as follows:

"The military and naval forces of the United States include (but are not necessarily limited to) the Army, the Navy, the Marine Corps, the Coast Guard, the Army Nurse Corps, female, the Navy Nurse Corps, female, the Women's Army Corps (the 'WACS'), the Women's Reserve Branch of the Naval Reserve (the 'WAVES'), the Women's Reserve Branch of the Coast Guard Reserve (the 'SPARS'), and the Marine Corps Women's Reserve. The term 'military or naval forces of any of the other United Nations' include any organization in the service of any one of such United Nations corresponding as nearly as may be to any of the enumerated organizations included in the military or naval forces of the United States."

FORMULA

- Item 1. Ascertain 1942 tax as shown on return which was due March 15, 1943.
- Item 2. Compute income tax and victory tax on 1943 income (on work sheet or on short form table which comes with declaration Form 1040ES, and later on final return, Form 1040 or 1040A). Servicemen exclude \$1,500 from service pay.¹²
- Item 3. Compare total 1943 tax (Item 2) with 1942 tax (Item 1).
- Item 4. *If 1943 Tax (Item 2) is Greater than 1942 Tax (Item 1).*
- (a) * Pay 1943 tax (Item 2).
 - (b) ** Pay also additional 25% of 1942 tax (Item 1). If, however, 1942 tax was less than \$66.67, then pay only the amount, if any, by which it exceeds \$50.
- Item 5. *If 1942 Tax (Item 1) is Greater than 1943 Tax (Item 2).*
- (a) *Civilians:*
 - (1) * Pay 1942 tax (Item 1).
** Pay also 25% of 1943 tax (Item 2.) If, however, 1943 tax is less than \$66.67, then pay only the amount, if any, by which it exceeds \$50.
 - (b) *Armed Forces:*
 - (1) Recompute 1942 tax as shown on 1942 return to exclude earned net income up to \$14,000.¹³
 - (2) * Pay such recomputed tax if it exceeds 1943 tax (Item 2)—if it does not, then pay 1943 tax (Item 2).
 - (3) ** Pay also 25% of 1943 tax (Item 2).
*** If, however, 1943 tax (Item 2) is less than \$66.67 then pay only the amount, if any, by which it exceeds \$50.

4. *Examples of Tax Resulting from Formula.*

1943 Tax Greater than 1942 (Item 4):

Both Civilians and Armed Forces:

¹² Passage of law appears certain, allowing post war victory tax credit for all purposes for 1943 irrespective of whether taxpayer has purchased bonds, insurance, etc. The above formula therefore does not include a technical qualification, as to use of such credit which would otherwise apply in isolated instances under § 36.1(a) of T. D. 5300, Oct. 1, 1943 (Fed. Reg., Oct. 5, 1943, p. 13454).

¹³ The method of such recomputation is explained more fully, *infra*, Sec. H.

* This is shown as Item 1 on declaration Form 1040ES. Amounts withheld from wages during year and amounts paid on 1942 tax are credited against this tax. The balance only is payable. If declaration is filed, payment is made September 15th and December 15th. Otherwise it is paid with March return.

** This additional amount is not shown on the declaration of estimated tax, but is only shown on the annual return on Form 1040 or 1040A which is filed in March, 1944. It may be paid in two installments, March, 1944 and March, 1945.

*** In exceptional cases where the amount of Item 5(b) (3) exceeds the smaller of the following, then the smaller of the following will be paid instead:

- (a) 25% of 1942 tax (Item 1).
- (b) The amount by which the 1942 tax (Item 1) exceeds \$50.

(Hypothetical Taxpayers' Situations, A, B, C, D, E, and F.)

	A	B	C	D
1943 Income and Victory Tax....	\$100	\$100	\$100	\$100
1942 Tax	0	12	54	80
Revised 1943 Tax	100	100	100	100
Addition to Tax (payable March, 1944 and 1945)	0	0	4	20

Total Tax for 1942 and 1943....\$100 \$100 \$104 \$120
1942 Tax Greater than 1943:

(a) *Civilians (Item 5-a):*

1942 Tax	\$100	\$100	\$100	\$100
1943 Income and Victory Tax....	0	12	54	80
Revised 1943 Tax	100	100	100	100
Addition to Tax (payable March, 1944 and 1945)	0	0	4	20

Total Tax for 1942 and 1943....\$100 \$100 \$104 \$120

(b) *Armed Forces (Item 5-b):*

	A	B	C	D	E	F
1942 Tax	\$100	\$100	\$100	\$100	\$100	\$100
1943 Income and Victory Tax....	0	10	60	60	80	80
Recomputed 1942 Tax	0	0	0	80	60	90
Revised 1943 Tax	0	10	60	80	80	90
Addition to Tax (payable March, 1944 and 1945)	0	0	10	10	20	20

Total Tax for 1942 and 1943....\$ 0 \$ 10 \$ 70 \$ 90 \$100 \$110

H. RECOMPUTATION OF 1942 TAX TO EXCLUDE EARNED NET INCOME UNDER SECTION 6(d)(1) OF CURRENT TAX PAYMENT ACT.¹⁴

In all cases where the 1942 tax is to be recomputed by servicemen under Section 6(d)(1) of the Current Tax Payment Act, the purpose is to ascertain how much of the 1942 tax was attributable to earned net income and to reduce it by that amount. In most situations the bulk of a taxpayer's 1942 income was earned income and it can be seen at a glance that the recomputation will reduce the 1942 tax to zero or certainly to less than the 1943 tax. If so, the 1943 tax is the one which is to be paid and there will be no need for an exact recomputation of the 1942 tax. However, in cases where the recomputation will still leave the 1942 tax greater than the 1943 tax an exact recomputation is necessary because the recomputed 1942 tax will be the one which will be reported and paid.

The factors to consider in making the recomputation will vary according to the type of returns used, as follows:

- (a) Recomputation of separate returns by single taxpayer.
- (b) Husband and wife who made separate returns for 1942.
 1. Where each will file separate return for 1943.
 2. Where they will file a joint return for 1943.
- (c) Husband and wife who made a joint return for 1942.

¹⁴The regulations relating to recomputation are set forth in T. D. 5300, Oct. 1, 1943 (FED. REG., Oct. 5, 1943, pp. 13452-13461) and in the case of estates, see: T. D. 5297, Sept. 20, 1943, (FED. REG., Sept. 23, 1943, p. 12931.)

1. Where they will file a joint return for 1943.

2. Where each will file separate return for 1943.

(d) Change of status during tax year (not treated herein).

It should be especially noted that in all cases where the 1942 tax can be recomputed, the earned net income to be eliminated is as defined in Section 25 (a) (4) of the Internal Revenue Code, to-wit:

"(C) 'Earned net income' means the excess of the amount of the earned income over the sum of the earned income deductions. If the taxpayer's net income is not more than \$3,000, his entire net income shall be considered to be earned net income, and if his net income is more than \$3,000, his earned net income shall not be considered to be less than \$3,000. In no case shall the earned net income be considered to be more than \$14,000."

(a) *Recomputation of Separate Returns by Single Taxpayer.*

Where the single taxpayer's 1942 return was made on the short form 1040A, the recomputation will in each case bring the 1942 tax down to \$00.00 in view of the fact that the net income shown on the short form could in no case exceed \$3,000 and would, therefore, all be considered "earned."

On the long return form 1040 the single serviceman, in making his recomputation, will merely compute again the 1942 tax, but eliminate all earned net income and report only items of unearned income. No earned income credit can be used in such recomputation. Also no deductions allocable to earned income, such as business expenses, can be taken.¹⁵

Example:

A single man had a \$16,000 salary and \$8,000 income from dividends in 1942. In 1943 he enters the armed services. In recomputing the 1942 tax he would show as income only the \$8,000 attributable to dividends, and the \$2,000 by which his salary exceeded the \$14,000 limitation on earned income. As this recomputation relates only to 1942, the \$1,500 exclusion cannot be taken. Assuming that he had no deductions, the original 1942 tax and the recomputed 1942 tax would be as follows:

Original 1942 Tax

<i>Income</i>	
Salary	\$16,000
Dividends	8,000
Total Income	\$24,000
Deductions—none	000
Net Income	\$24,000
Less personal exemption	500
Balance (surtax net income)	\$23,500
Less earned income credit	1,400
Balance subject to normal tax	\$22,100

¹⁵ See: INT. REV. CODE § 25 (a) (4) (B).

Normal tax (6%)	\$ 1,326
Surtax (see surtax tables on return form)	7,720
Total original 1942 tax	\$ 9,046

Recomputed 1942 Tax

Income

Salary (excess over \$14,000)	\$ 2,000
Dividends	8,000
Total Income	\$10,000
Deductions—none	000
Net Income	\$10,000
Less personal exemption	500
Balance (surtax net income)	\$ 9,500
No earned income credit allowable in recomputation	000
	\$9,500
Normal tax (6%)	\$ 570
Surtax (see surtax tables on return form)	1,880
Total recomputed 1942 tax	\$ 2,450

As shown in the formula in the preceding section, if the man's recomputed 1942 tax of \$2,450 is greater than his 1943 tax, then the recomputed amount will be shown as the estimated tax for 1943 on the declaration, if filed, and also on the final return. If the recomputed tax is less than the 1943 tax, the 1943 tax will be shown. The additional 25% will apply to the 1943 tax (as it was the lower year before recomputation). Such addition will only be shown on the final return and will be paid in full on March 15, 1944, or in equal installments March 15, 1944 and March 15, 1945.

(b) *Recomputation by Husband and Wife Who Made Separate Returns for 1942.*

(1) *Where each will file separate return for 1943.*

In this situation only the spouse who is a member of the armed forces may recompute his 1942 tax, if it is the higher of the two years, and it will be done in the same manner as shown above for a single taxpayer. However, it should be noted that where such taxpayer claimed a part of the \$1,200 married exemption on his 1942 return, Form 1040,¹⁶ a considerable amount of tax can sometimes be saved by filing amended 1942 returns on which the person in the service will claim none of the personal exemption and allow his spouse to take the

¹⁶ Where separate returns for 1942 were filed on the short return form 1040A, the above suggested amendment is not possible because the personal exemption is included in the tax tables and is not separately deductible. Also an amendment cannot be made from form 1040A to form 1040.

whole personal exemption for 1942 on her amended return.^{16a} The reason for this is that, because of the right to recompute, the total tax for 1942 and 1943 of the person in the service is not increased by an increase in the tax for 1942 alone, as long as all of such tax is attributable to earned net income. Technically when such amended returns are filed, one-half of the additional 1942 tax resulting from the amendment of the husband's return should be paid plus 6% interest per annum from March 15, 1943, to the date upon which it is paid, because one-half of such addition became due prior to September 1, 1943, the date upon which the 1942 tax was cancelled. In addition to the right to elect how much of the personal exemption will be claimed by a spouse, either husband or wife may claim the credit for a dependent, where the support to such dependent is furnished from community income. In such case the Collector of Internal Revenue at Tacoma has ruled that the credit for dependents may also be shifted from one spouse to another when amended returns are filed.

(2) Where they will file a joint return for 1943.

Where separate returns were filed in 1942 by a serviceman and his wife, and a joint return is to be filed for 1943, the method of recomputing tax is governed by Section 6(d)(2) of the Current Tax Payment Act which reads as follows:

"(2) Joint Returns:—If the taxpayer either for the taxable year 1942 or for the taxable year 1943 makes a joint return with his spouse, the taxes of the spouses for the taxable year for which a joint return is not made shall be aggregated for the purposes of subsections (a), (b), and (c), and in case the taxable year for which a joint return is not made is the taxable year 1943, the liability for the increase in the tax for the taxable year 1943 under subsections (b) and (c), shall be joint and several."

By virtue of the above section, the taxpayers in such a case must first aggregate their separate 1942 taxes and compare the total with the tax for 1943, as shown on a joint return. If the aggregate tax for 1942 is greater than the tax for 1943, then a recomputation is made with respect to the husband's separate 1942 return. If, after such recomputation, the aggregate of his recomputed 1942 tax plus his wife's 1942 tax is still greater than the 1943 tax, such aggregate will be paid. Otherwise, the 1943 tax will be paid. In any event, the 25% additional will apply to the 1943 tax. The possibility of tax saving, by first amending the 1942 returns to let the wife take the whole personal exemption, is the same as set forth in the preceding paragraph.

^{16a} The Collector of Internal Revenue has assumed that amended returns are necessary in order to allow the wife to claim the benefit of more of the \$1,200 personal exemption on her 1942 tax than was originally claimed when the 1942 returns were filed. Although such assumption appears to be logical, it is possible that the Treasury may allow such adjustment to be made at the time the final 1943 return is prepared without the necessity of actually preparing and filing amended 1942 returns.

(c) *Husband and Wife Who Made a Joint Return for 1942.*

The Treasury Department has ruled¹⁷ that in recomputing a joint 1942 return, where one of the spouses is in the service, the recomputation is to be made by eliminating only the earned net income allocable to that spouse who is in the service. Although this decision appears to be equitable and avoids an otherwise large discrepancy between different types of 1942 returns, it is the writer's opinion that there is some question as to whether it is authorized by the wording of the law, Section 6(d)(1). Section 6(d)(1) states, in effect, that the 1942 tax shall be reduced by an amount "equal to the amount by which *the* tax for the taxable year 1942 * * * is increased by reason of the inclusion in *the* net income for the taxable year 1942 of the amount of *the* earned net income." The wording does not say that the earned net income to be eliminated shall be income earned or owned by the serviceman in question. In view of the fact that the taxpayer filed a joint return with his spouse for the year 1942, he was jointly and separately liable for the whole 1942 tax. It would seem, therefore, that a court might well hold that the earned net income by virtue of which *the* 1942 tax was increased, means the earned net income on the 1942 joint return, irrespective of what portion of such income was earned or owned by the taxpayer in question, prior to making the 1942 return.

It should be also noted that in recomputing a joint 1942 return, an earned income credit is allowable only in an amount equal to the excess, if any, of the earned income credit allowable on the 1942 return, over an amount equal to 10% of the serviceman's "earned net income" for 1942. Thus, if a serviceman had \$2,500 of earned net income and \$500 of unearned net income for 1942 and his wife had \$2,000 earned net income, their 1942 earned income credit would be 10% of the total earned net income, or \$450. However, as the husband's net income was only \$3,000, all of it will be considered as earned net income for purposes of recomputation, and, on the recomputed 1942 joint return the allowable earned income credit would be the excess, or \$150.

(1) *Where they will file joint return for 1943.*

Subject to the comments set forth in the preceding two paragraphs, the 1943 tax as computed on the joint return will be compared with the joint 1942 tax. If the latter is greater, then it will be recomputed by eliminating the earned net income of the serviceman only.

(2) *Where each will file separate returns for 1943.*

In this situation the taxpayer must under Section 6(d)(2) compare the aggregate tax for 1943 with the tax shown on the joint 1942 return, as previously set forth in paragraph H(b)(2) above. If the joint 1942 tax is greater than the aggregate 1943 tax, the 1942 tax is recomputed to eliminate the serviceman's earned net income. If the recomputed

¹⁷ Sec. 36.4 T. D. 5300 (FED. REG., Oct. 5, 1943, p. 13458).

1942 tax is greater than the 1943 aggregate tax as shown on separate returns such recomputed 1942 tax will be payable, and the difference may be divided between the spouses on their 1943 returns in such manner as they agree, although they are jointly and severally liable for such difference (Section 36.5 T. D. 5300).

I. DECLARATIONS AND CREDITS AGAINST TAX.

The fact that a joint or separate declaration of estimated tax is filed, does not in any way affect the right to file such type of final return as is desired, although taxpayers filing a joint declaration are jointly and separately liable for the amount of estimated tax shown thereon. A joint declaration has one advantage, in that credits may be used against tax for 1942 installments which were paid by both the husband and wife where separate 1942 returns were filed. This would not be true if separate declarations were filed.

If a joint return was filed for 1942, but separate declarations or returns are made in 1943, husband and wife must each report the amount of their 1943 tax. However, Section 19.58-3 of T. D. 5297 provides that the excess of the joint 1942 tax over the aggregate separate 1943 taxes may be divided between them as they agree for purposes of reporting it on the declarations.

Payments made with respect to tax liability shown on a 1942 joint return may, if separate declarations or returns are made for 1943, be applied against the estimated tax of either spouse or may be divided between them in any manner they see fit (Section 36.10 T. D. 5300).

J. ABATEMENT OF TAX FOR MEMBERS OF ARMED FORCES UPON DEATH.¹⁸

Section 8 of the Current Tax Payment Act provides for abatement of certain taxes upon death of members of the armed forces and reads as follows:

"Section 8. Abatement of Tax for Members of Armed Forces Upon Death.

"Chapter 1 of the Internal Revenue Code is amended by inserting after section 404 the following new supplement:

"Supplement U—Abatement of Tax for Members of Armed Forces Upon Death.

"Sec. 421. Abatement of Tax for Members of Armed Forces Upon Death.

"In the case of any individual who dies on or after December 7, 1941, while in active service as a member of the military or naval forces of the United States or of any of the other United Nations and prior to the termination of the present war as proclaimed by the President, the tax imposed by this chapter shall not apply with respect to the taxable year in which falls the date of his death, and the tax under this chapter and under the corresponding title

¹⁸ Regulations in T. D. 5297, Sept. 20, 1943 (Fed. Reg. Sept. 23, 1943, p. 12923 *et seq.*

of each prior revenue law for preceding taxable years which is unpaid at the date of his death (including interest, additions to the tax, and additional amounts) shall not be assessed, and if assessed the assessment shall be abated, and if collected shall be credited or refunded as an overpayment.'"

The above provision applies to members of the military or naval forces with respect only to death occurring during active service. In such case all unpaid tax is forgiven irrespective of the source of income which resulted in the tax. The benefit applies also irrespective of the cause of death. It can easily be seen that this provision may result in a very large tax saving where the taxpayer is in a high income tax bracket, and it may indirectly encourage the postponement of tax payment so long as is possible. While most taxpayers in the service prefer to keep their taxes paid up to date, still in cases where the tax is large they may consider postponing payment, if possible, meanwhile investing the amount involved, so as to benefit their dependents in the event of death.

JJ. WITHHOLDING

Both the victory tax¹⁹ and the Current Tax Payment Act²⁰ exempted "wages for services performed as a member of the military or naval forces of the United States, other than pensions and retired pay" from the withholding provisions. The Commissioner of Internal Revenue has ruled that under the above provision, withholding will not apply to active service pay or to extra pay received by enlisted personnel from post exchanges or ship's service departments.

It should be noted that under the withholding provisions of the Current Tax Payment Act a spouse may claim the whole married exemption of \$24 per week by filing a certificate on form W4 with the employer. Employed wives of servicemen should therefore claim the whole exemption, unless they decide that withholding is desirable in order to accrue a credit for future income tax liability.

The fact that the husband or wife may have chosen to claim the whole personal exemption for purposes of withholding does not preclude them from splitting the regular \$1,200 personal exemption, in such manner as they choose, for purposes of making income tax estimates or returns.

In preparing tax estimates and final returns a credit on the amount to be paid is given for amounts withheld from wages during the year. The credit against tax for amounts withheld on community income of one spouse may be divided equally between a husband and wife who file separate returns.

¹⁹ INT. REV. CODE § 465 (b) subchapter D of Chap. I; Revenue Act of 1942 § 172 (a).

²⁰ Current Tax Payment Act of 1943 § 2; INT. REV. CODE § 1621 (a) subchapter D of c. 9.

K. POSTPONEMENTS.

Special postponements in favor of servicemen (and to some extent, their wives) have been provided by law or authorized by regulation in several situations. A summary of the available postponements, with citations of the applicable authority, should suffice for purposes of this article.

1. *Sea Duty or Outside United States (T. D. 5279).*

The right to postponement of the filing of declarations or returns and the payment of tax where a serviceman is on sea duty or outside the continental United States, is exhaustively treated in T. D. 5279.²¹ Space only permits a summary of the most important provisions set forth therein. The postponements provided with respect to estates, petitions, claims, refunds, assessments or collections, are not treated.

In the case of members of armed forces serving on sea duty or on duty outside continental United States (the 48 States and District of Columbia) the date for making declarations, returns or payments of tax, which become due while on such duty (or which become due within 90 days after such duty where duty was continuous for over 91 days) is postponed until the 15th day of the fourth month after the month in which such person ceases to be a member of the military or naval forces of the United States serving on sea duty or outside continental United States, or unless the war ends at an earlier date. Before the new due date such member should file the return, payment, etc., with a letter explaining the delay. For purposes of these postponements, members of the armed forces are considered to include the Army, Navy, Marine Corps, Coast Guard, Army Nurse Corps, Female, WAC, Navy Nurse Corps, Female, WAVES, SPARS, Marine Corps Women's Reserve, and commissioned officers of the Coast and Geodetic Survey and the Public Health Service.

Where the husband's declaration, return or tax is postponed under the above paragraph, the wife is granted the same postponement if her annual gross income is less than \$1,200. However, if the wife has a gross income of \$1,200 or more, she must file such declaration or return and pay tax, but such filing does not preclude a later amendment or filing of a joint return when her husband returns. With respect to returns and declarations of estimated tax for the year 1943, however, the spouse (if her income is over \$1,200 and if a joint return was filed for 1942) is not required to include in her return or declarations the *increases in the 1943 tax*, which result from the required comparison between the joint 1942 tax and the joint or aggregated taxes for 1943. Such increases may be reported and paid with amended declarations or returns on or before the serviceman's postponed due date.

Where husband and wife are domiciled in a community property

²¹ T. D. 5279, July 10, 1943 (FED. REG., July 14, 1943, pp. 9602-9614) issued under authority of INT. REV. CODE §§ 3804, 3805 and 3791.

state and the husband's tax is postponed, the wife's portion of community income may be excluded from the returns which she must file, if such community income is neither actually or constructively received by her. For this purpose receipt of income by the husband does not constitute "constructive receipt" by the wife. If the wife excludes such community income from her return, she is required later to include it in an amended return before the last day on which the husband may file.

2. *Soldiers' and Sailors' Civil Relief Act.*

Under Section 513 of the Soldiers and Sailors' Civil Relief Act,²² *payment* (but not filing declarations or returns) may be deferred during military service, and six months thereafter, if ability to pay is impaired by reason of service in the armed forces. Preferably an application for such deferment should be filed with the return or declaration prior to the due date. Such application should indicate the period of the service and the change in ability to pay the tax, resulting from entry into the service. Forms of application may be obtained from the Collector's office. The Collector may require further proof as to impairment of such ability, but, at least where a large amount of tax is not involved, the applications are granted nearly as a matter of course. No penalty or interest accrues for deferments allowed under the act.

The above benefit does not inure to the wife of the person in military service and, in the case of a joint return, the wife is required to pay the portion of the tax attributable to her net income.

In addition to the above, section 700²³ of the Soldiers' and Sailors' Civil Relief Act authorizes application to courts for relief in respect to obligations for taxes and assessments whether falling due prior to or during the military service.

The terms "persons in military service," "military service" and "active service," as used for purposes of the Soldiers' and Sailors' Civil Relief Act is defined, as follows, in Sec. 101(1):

"The term 'persons in military service' and the term 'persons in the military service of the United States,' as used in this Act, shall include the following persons and no others. All members of the Army of the United States, the United States Navy, the Marine Corps, the Coast Guard, the Women's Army Auxiliary Corps, and all officers of the Public Health Service detailed by proper authority for duty either with the Army or the Navy. The term 'military service,' as used in this Act, shall signify Federal Service on active duty with any branch of service heretofore referred to or mentioned as well as training or education under the supervision of the United States preliminary to induction into the military service. The term 'active service' or 'active duty' shall include the

²² Pub. L. No. 861, 76th Cong., Oct. 17, 1940; Pub. L. 554, 77th Cong., May 14, 1942; Pub. L. No. 732, 77th Cong., Oct. 6, 1942, and Pub. L. No. 753, 77th Cong., Oct. 21, 1942; 50 USC § 510 *et seq.*

²³ Pub. L. 732, 77th Cong., Oct. 6, 1942.

period during which a person in military service is absent from duty on account of sickness, wounds, leave, or other lawful cause."

"WAVES" are included because they actually are members of the Navy.

3. *Payment of June 15, 1943, Installment.*

Attorneys may discover that their clients in the service did not pay the second installment of the 1942 tax which was due on June 15, 1943. The deferment of such payment was authorized by instructions issued by the Army and Navy with the concurrence of the Commissioner of Internal Revenue, but only upon the conditions set forth in the instructions, which read as follows:

"If it is estimated that no liability for income tax plus victory tax will accrue on 1943 income, the June 15, 1943, payment need not be made provided member of the armed forces upon receipt of statement covering June installment immediately notifies the Collector of Internal Revenue from whom statement received:

"(1) That he is a member of the armed forces.

"(2) That his tax liability on 1943 income is estimated to be zero, and

"(3) That his tax liability for the year 1942 recomputed after excluding all earned income up to \$14,000 (with first \$3,000 income from any source considered as earned income) is not in excess of amount already paid in 1943, and

"(4) That he will file a declaration of estimated tax for 1943 by September 15 and will make such payment as is required."

4. *Extension of Time for Filing September 15 and December 15 Declarations of Estimated Tax.*²⁴

The Commissioner of Internal Revenue granted to members of the military and naval forces an extension to March 15, 1944, for filing the declarations of estimated tax which would otherwise have been required on September 15, 1943 and December 15, 1943. The extension applies irrespective of whether the taxpayer paid his June 15, 1943, installment. It does not apply to spouses of the persons in the service. However, informal indications are that it will be construed to apply to spouses, to the same limited extent which is applicable to spouses of persons in the armed forces who are on sea duty. See Section K(1), *supra*.

As used in connection with this extension the term "member of the military or naval forces of the United States" includes:

"any individual in the Army of the United States, the United States Navy, the Marine Corps, the Coast Guard, the Army Nurse Corps, Female, the Women's Army Corps, the Navy Nurse Corps, Female, the Women's Reserve branch of the Naval Reserve, the Women's Reserve branch of the Coast Guard Reserve, and the Women's Reserve branch of the Marine Corps Reserve (Marine Corps Women's Reserve),

²⁴ T. D. 5291, Aug. 21, 1943; (FED. REG., Aug. 24, 1943, p. 11650.)

and any commissioned officer of the Coast and Geodetic Survey or of the Public Health Service."

L. INCOME FROM UNITED STATES POSSESSIONS.

In view of the fact that many servicemen have been stationed in possessions of the United States, a summary of the provisions of Section 251 of the Internal Revenue Code may be of assistance in some cases. Ordinarily, income received by a citizen who is domiciled in the United States constitutes a part of gross income, irrespective of where it was earned or received. However, with respect to some types of income received while stationed in possessions, a special rule is applicable under Section 251.

There may be excluded from gross income the compensation derived from sources within a United States possession (Puerto Rico, the Philippine Islands, the Panama Canal Zone, Guam, American Samoa, Wake, Palmyra, Johnston and the Midway Islands) and received by the taxpayer outside the United States (the States, the Territories of Alaska and Hawaii, and the District of Columbia), if the taxpayer can show—

- (1) That for the 3-year period immediately preceding the close of the taxable year, or for such part of such period as may be applicable, 80 per cent of his gross income was derived from sources within a possession; and
- (2) That 50 per cent or more of his gross income (computed without the benefit of this provision) for such period or part of period was derived from the active conduct of a trade or business within a possession, either on his own account or as an employee or agent of another.

The "source" of the compensation is the place where the services are rendered. Compensation paid by the United States to its military and naval personnel for services rendered in a possession represents income derived from a business within a possession. An individual serving outside the continental United States is deemed to receive his entire pay at his station regardless of allotments made by him.

Citizens entitled to the benefits of Section 251 are required to file a schedule on Form 1040E, except where they have no income from sources within the United States and receive no income within the United States.

M. REFUNDS.

Many members of the armed forces will have a right to a refund because they will have credits arising from payments previously made for the 1942 tax, but will not have any final tax liability for both 1942 and 1943, or any estimated future tax liability for 1944. Refunds to servicemen may be automatic upon the filing of the final return due March 15, 1944. However, under the regulations as they now exist claims for refunds are made on Form 843. The claim should ordinarily have attached thereto a copy of the return form which shows the credit for which the claim is made, and should set forth in detail each ground upon which a refund is claimed and sufficient facts to explain the basis therefor.